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**BEFORE THE PUBLIC UTILITIES COMMISSION**
**OF THE STATE OF CALIFORNIA**

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| In the Matter of the Application of San Diego Gas & Electric Company and Southern California Gas Company for Authority to Integrate Their Gas Transmission Rates, Establish Firm Access Rights, and Provide Off-System Gas Transportation Services. | A.04-12-004 (Phase II) |

# SOUTHERN CALIFORNIA GENERATION COALITION APPLICATION FOR REHEARING

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Dated: January 16, 2007

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**SOUTHERN CALIFORNIA GENERATION COALITION**
**APPLICATION FOR REHEARING**

In accordance with Rule 16.1 of the Rules of Practice and Procedure of the California Public Utilities Commission ("Commission" or "CPUC"), the Southern California Generation Coalition ("SCGC") respectfully requests rehearing of Decision ("D.") 06-12-031 (Dec. 14, 2006), mailed on December 15, 2006, in the captioned proceeding. D.06-12-031 approves with modifications Southern California Gas Company ("SoCalGas") and San Diego Gas & Electric Company's ("SDG&E") (collectively, "SoCalGas") flawed proposal to sell "firm access rights" to the receipt points on their system.

## I. INTRODUCTION.

The system of firm access rights ("FAR") and associated access charges that was approved by the Commission in D.06-12-031 is beyond the Commission's jurisdiction. Furthermore, the Commission has utterly failed to provide a rational basis for approving FAR. The FAR program is unnecessary and unsupported by the record. The findings of fact that are intended to support the adoption of the FAR program are either irrelevant or conclusory and do not support the imposition of a new, costly system of receipt point access rights that are unconnected to any sort of intrastate transportation service. Finally, many of the specific features of the FAR program are discriminatory or arbitrary and capricious and, thus, are contrary to law. From the Commission's tenuous analysis of the need for a system of FAR to its analysis of each proposed feature of FAR, the Commission fails to provide any insight into the logic of its conclusions. The Commission clearly had a result it wanted to reach and reached that result without basing its determinations on the evidence presented in this proceeding. Rehearing should be granted, and the FAR program should be rejected.

The specific grounds for rehearing are as follows:

- The FAR access charge is outside of the Commission's jurisdiction and, thus, is illegal.
- There is no rational basis or record support for establishing a system of FAR.
- There is no rational basis for establishing set-asides nor a coherent method to granting individual set-asides. Thus, the set-asides are discriminatory, arbitrary and capricious, and contrary to law.
- Although D.06-12-031 rejects set-asides for noncore customers including gas-fired electric generators ("EGs") that have long-term commitments to interstate pipeline capacity, the Decision relies upon the fact that EGs receive set-asides as justification for maintaining a preference for annual bids over seasonal bids in Step 2 of the FAR bidding process.
- There is no record support for reserving receipt point capacity for non-end-use customers in Step 3 of the FAR bidding process. Thus, the limitations on capacity to be made available in Steps 1 and 2 are arbitrary and capricious and are contrary to law.
- D.06-12-031 fails to limit bids for existing capacity in Step 3 to three-year terms.

- The five-cent "unbundled" access charge is not based on any cost evidence, is arbitrary and capricious, and is contrary to law.
- D.06-12-031 prejudges the next SoCalGas Biennial Cost Allocation Proceeding ("BCAP") by predetermining that the supposed "regulatory gap" shall be closed through a rate design that imposes demand charges on noncore customers.
- D.06-12-031 conflicts with California's greenhouse gas ("GHG") emissions policy.

Upon rehearing, SCGC respectfully requests that the Commission do the following:

- Reject SoCalGas' FAR proposal in its entirety.
- If FAR is not rejected, revise D.06-12-031 to set forth findings of fact and conclusions of law that provide a rational basis for approving a system of firm rights.
- If the Commission, upon rehearing, revises D.06-12-031 to set forth findings of fact and conclusions of law that provide a rational basis for approving a system of firm transportation rights:
  (1) define the purpose for which set-asides should be established and establish a non-discriminatory method for determining set-asides, or eliminate set-asides altogether;
  (2) reject the preference for annual bids over monthly bids in Step 2;
  (3) eliminate the arbitrary five-year average limitation on the amount of capacity that shall be made available in Steps 1 and 2 of the FAR bidding process;
  (4) limit the term of contracts for existing capacity awarded in Step 3 to three years;

(5) eliminate the five-cent "unbundled" access charge; and

(6) make it clear that D.06-12-031 is not predetermining the outcome of SoCalGas' and SDG&E's next BCAP proceedings.

## II. THE FAR ACCESS CHARGE IS OUTSIDE THE COMMISSION'S JURISDICTION AND, THUS, IS CONTRARY TO LAW.

The Commission's decision to implement a charge to gain access to SoCalGas' intrastate transmission system is inconsistent with Federal Energy Regulatory Commission ("FERC") findings regarding a similar access charge. Thus, the Decision reaches beyond the Commission's jurisdiction and is contrary to law.

D.06-12-031 fails to adequately explain how the access charge in this proceeding is distinguishable from the Wheeler Ridge access charge found to be illegal in *Union Pacific Fuels, Inc., et al. v. Southern California Gas Co., et al.*, 76 FERC ¶ 61,300 (1996), *reh'g den.*, 77 FERC ¶ 61,283 (1996), *aff'd in part sub nom, Public Utils. Comm'n of the State of Cal. v. FERC*, 143 F.3d 610 (D.C. Cir. 1998), *on remand*, 85 FERC ¶ 61,177 (1998) ("*Union Pacific Fuels*"). Although the Commission attempts to distinguish the FAR access charges at issue in this proceeding from the Wheeler Ridge access charge in *Union Pacific Fuels*, the FAR charges have the same fundamental flaws as the Wheeler Ridge charges. Finding of Fact 29 asserts that the FAR reservation charge is different from the access charge addressed in *Union Pacific Fuels*. D.06-12-031 at 136. However, Finding of Fact 31 unequivocally admits: "The FAR reservation charge provides the FAR holder with *access* to the transmission system" just like the Wheeler Ridge access charge. D.06-12-031 at 136 (emphasis added).

The FERC has already addressed the legality of SoCalGas charging access fees to interstate pipeline shippers for the right to nominate deliveries of gas into SoCalGas. In 1993, SoCalGas proposed to assess an access charge on interstate shippers on Kern River Gas

Transmission Company ("Kern River") and Mojave Pipeline Company ("Mojave") that desired to nominate deliveries of gas into SoCalGas at the then-new Wheeler Ridge receipt point. The CPUC approved the charge. *See* Resolution G-3072. Interstate pipeline shippers filed complaints at the FERC raising the issue of "whether the CPUC authorizing SoCal to assess an interconnection charge to shippers on interstate pipelines who deliver gas to SoCal encroached upon the [FERC's] exclusive jurisdiction over the transportation of gas in interstate commerce." *Union Pacific Fuels, Inc., et al. v. Southern California Gas Company, et al.*, 76 FERC ¶ 61,300, *slip op.* at 9 (Sep. 19, 1996).

The FERC found that the charge violated the Natural Gas Act ("NGA") "because the charge, as conceived by the CPUC, is a charge to interstate shippers for the act of moving gas over the Kern/Mojave pipeline and delivering it to SoCal rather than a charge for any service performed by SoCal after its receipt of the gas." *Id.* at 10. "This is demonstrated by the fact that the charge applies to the interstate customers of Kern/Mojave who deliver gas to SoCal, regardless of whether those shippers have service agreements with SoCal for the transportation of that gas over the SoCal Gas system after its receipt." *Id.* The Commission granted the complaints filed by the interstate pipeline shippers.

Subsequently, the FERC issued an order denying rehearing. *Union Pacific Fuels, Inc., et al. v. Southern California Gas Company, et al.*, 77 FERC ¶ 61,283 (Dec. 19, 1996) ("Order Denying Rehearing"). On rehearing, the FERC stated that the SoCalGas access charge "in its current form, sweeps too broadly. That is because the charge would apply even to an interstate shipper which has no service agreement with SoCal for the transportation of gas over SoCal's facilities and only ships gas over the Kern/Mojave interstate pipeline for the purpose of delivering it to SoCal." *Id.*, *slip op.* at 4. The FERC noted that, "with relatively minor changes to the interconnection charge, the CPUC could avoid infringing on [FERC's] exclusive jurisdiction …." *Id.* "The CPUC need only change the applicability of the incremental charge to those customers of SoCal who have service agreements for the actual transportation of natural gas over the new interconnection facilities." *Id.*

On appeal, the Court affirmed FERC's reasoning and conclusions, noting that the fact that intrastate shippers also had to pay the charge "has no bearing on whether the tariff was indeed an access charge to interstate shippers." 143 F.3d at 614. In upholding the FERC's exercise of jurisdiction over the Wheeler Ridge access charge, the Court stated: "In functional terms, a charge to interstate shippers for access to intrastate service directly and significantly affects interstate shipment of gas by increasing its cost. The access charge thus fell squarely within FERC's regulatory bailiwick both in legal and policy terms." *Id*. at 615.

In an attempt to quickly dispense with the legality of the FAR reservation charge, the Commission tries to distinguish the FAR reservation charge from the Wheeler Ridge access charge by claiming that the FAR reservation charge is a charge for transportation service:

> The reservation charge under the two FAR proposals is assessed on those market participants who have a FAR at a receipt point on the SDG&E and SoCalGas transmission system. The holder of the FAR has the firm right to have its gas transported over the transmission system to the citygate. The reservation charge at issue is being assessed for the right to access the SDG&E and SoCalGas receipt point, and to have the gas transported over the transmission system of SDG&E and SoCalGas. We therefore conclude that the reservation charge is not unlawful under the holding of *Union Pacific Fuels*.

D.06-12-031 at 73-74. Notwithstanding the Commission's attempt to tie intrastate transportation service to the FAR right of access into SoCalGas' system, the FAR reservation charge is truly an access charge rather than a charge for any intrastate transportation service.

Three important facts belie the Commission's attempt to distinguish the FAR charges from the Wheeler Ridge access charge by claiming the FAR charges are actually charges for transmission service. First, there is already an existing citygate market in which intrastate shippers, marketers, and end-use customers have the option of purchasing gas at every receipt point. The new "citygate" is merely a paper point created to justify charging market participants a five-cent access charge. SoCalGas' proposed tariff makes it clear that the access charge will be assessed against volumes of gas delivered into the system at delivery points that are paper points: an intrastate transportation agreement, a Citygate Pool Account, a Storage Account or a Contracted Marketer or a Core Aggregator account. *See* Proposed Schedule No. G-RPA, Sheet 2. These paper delivery points show that the FAR reservation charge is a charge solely for accessing the SoCalGas system rather than for any actual intrastate transportation, just as was the case with the Wheeler Ridge access charge. The Commission is merely creating a paper delivery point and requiring interstate shippers that want to "access" the southern California market to acquire the right to deliver gas to the new paper point rather than at the interconnection with SoCalGas and the interstate transportation system.

Second, as discussed further below, the Commission is "unbundling" only five cents from the transportation rate, despite the fact that the transportation supposedly associated with the FAR access right costs closer to 15.75 cents/dth, which the Commission acknowledged approximates SoCalGas system backbone transmission costs. D.06-12-031 at 85. If actual transportation service were associated with the firm access rights, the Commission would be requiring end-use customers that are currently bearing the cost of the SoCalGas transmission system to subsidize the customers that would be holding FAR. On the other hand, if, as is the case here, there is no actual transportation associated with firm access rights, then the holders of

FAR are subsidizing transportation used by end-use customers. Either way, the Commission's choice of five cents for an access charge clearly shows that there is no actual transportation associated with FAR.

Third, the Commission declined to allocate any fuel costs to the transportation service that would supposedly be provided to FAR holders, stating that fuel costs are recovered from core and noncore customers in their transportation rates. D.06-12-031 at 83. If FAR holders were actually receiving some transportation service, the shippers that hold FAR that ship gas to the new citygate would be receiving a service without bearing all the costs of that service. However, given that the new "citygate" is merely a paper point, there is no actual transportation provided to the FAR holder, and an in-kind fuel charge is unjustified.

In D.06-12-031, the Commission attempts to create some nexus between deliveries of gas into SoCalGas' system with some intrastate transmission service in an attempt to distinguish the FAR access charge from the Wheeler Ridge access charge. The nexus is a sham.

The Commission should grant rehearing, reject the sham, and reject the FAR access charges as beyond the Commission's jurisdiction.

## III. D.06-12-031 FAILS TO PROVIDE A RATIONAL BASIS FOR APPROVING THE FAR SYSTEM.

Section 1705 of the Public Utilities Code requires that Commission decisions "shall contain, separately stated, findings of fact and conclusions of law by the [C]ommission on all issues material to the order or decision." The separately stated findings of fact and conclusions of law "afford a rational basis for judicial review and assist the reviewing court to ascertain the principles relied upon by the [C]ommission and to determine whether it acted arbitrarily, as well as assist parties to know why the case was lost and to prepare for rehearing and review, assist others planning activities involving similar questions, and serve to help the [C]ommission avoid careless or arbitrary action." *Greyhound Lines, Inc. v. Public Utilities Commission* (1967) 65 Cal.2d 811, 813; 56 Cal.Rptr. 484, 485; 423 P.2d 556, 557; *California Motor Transport Co. v. Public Utilities Commission* (1963) 59 Cal.2d 270, 274-275; 28 Cal.Rptr. 868, 871; 379 P.2d 324; *California Manufacturers Association v. Public Utilities Commission* (1979) 24 Cal.3d 251, 258-259; 155 Cal.Rptr. 664, 667-668; 595 P.3d 98, 101-102.

"Every issue that must be resolved to reach that ultimate finding is 'material to the order or decision' and findings are required on the basic facts upon which the ultimate finding is based." *Greyhound Lines, Inc. v. PUC, supra,* 65 Cal.2d 811, 813; *California Motor Transport Co. v. PUC, supra,* 59 Cal.2d 270, 274-275; *City of Los Angeles v. Public Utilities Commission* (1972) 7 Cal.3d 331, 337; 102 Cal.Rptr. 313, 318; 497 P.2d 785, 790. Although the Commission may have the discretion to determine which factors are relevant to a particular decision, the Commission must state those factors and make findings on the material issues that ensue from those factors. *California Motor Transport Co. v. PUC, supra,* 59 Cal.2d 270, 275; *City of Los Angeles v. PUC, supra,* 7 Cal.3d 331, 337.

In applying Section 1705, the Supreme Court has invalidated Commission decisions which failed to make findings on every issue that was necessary to reach the ultimate finding. *Greyhound Lines, Inc. v. PUC, supra,* 65 Cal.2d 811, 813 (ultimate finding regarding "public interest"); *California Motor Transport Co. v. PUC, supra,* 59 Cal.2d 270, 274-275 (ultimate finding regarding "public convenience and necessity"). For example, in *California Manufacturers Association v. Public Utilities Commission*, *supra*, 24 Cal.3d 251, 258-259 ("*CMTA*"), the Commission adopted a certain rate design based upon findings that the adopted rate design would encourage conservation of natural gas and that conservation would be beneficial. However, the Supreme Court annulled the decision because the Commission's findings failed to show that the adopted rate design would be more likely to result in conservation than other proposed rate designs.

D.06-12-031 patently fails to meet the requirement of Section 1705 that there must be separately stated findings of fact resolving all issues that are material to reaching the ultimate finding that now "[t]he time is ripe to adopt a system of FAR for southern California." Finding of Fact 15, D.06-12-031 at 134. Conclusory findings of fact that lack supporting facts should be rejected, particularly where, as here, the Commission is fundamentally changing the nature of transmission rights on SoCalGas' system and interferring with the nominations and deliveries on interstate pipelines. D.06-12-031 fails to abide by the requirement that the Commission provide a rational basis for its decisions.

### A. D.06-12-031 Fails to Rely on Record Evidence in Finding that There Is a Need for a System of FAR.

In its attempts to justify a need for FAR, the Commission relies on several irrelevant or conclusory facts (*i.e.*, ultimate facts not supported by any basic facts). The Commission mischaracterizes the reliability of access to the SoCalGas system and erroneously contends that because FAR schemes of one sort or another have been considered over the past nine years, now is the time to adopt a FAR system. The Commission erroneously contends that there is no citygate market in southern California and erroneously concludes that because Pacific Gas and Electric Company's ("PG&E") "FAR-type" system is working fine, a FAR system should be adopted for SoCalGas. The evidence relied upon by the Commission is insufficient to support its conclusion that a system of FAR should be implemented on SoCalGas. Indeed, the record shows that SoCalGas' system is working well and that FAR will result in less flexibility than customers currently enjoy without providing any additional security.

The Commission relies on the following findings of fact in support of establishing a FAR system:

7. Due to the difference between the delivery capability of the upstream gas supplies and the takeaway capacity of the receipt points on the SDG&E and SoCalGas integrated transmission system, problems in the delivery of gas can result.

8. Under the current system of allocating capacity on the SDG&E and SoCalGas transmission system: (1) end use customers are the only ones who can transport gas; (2) SoCalGas allocates the available receipt point capacity to the upstream pipelines daily; and (3) the upstream interstate pipelines allocate the capacity among their shippers using their FERC-approved capacity allocation rules.

9. The current system of capacity allocation can result in a situation where access to the system is available only on an interruptible basis, shippers' gas supplies are pro-rated, and receipt points are constrained.

15. The time is ripe to adopt a system of FAR for southern California.

16. The basic underlying system of firm tradable transmission rights has worked and functioned well in northern California.

18. Although capacity constraints have not been much of a problem during the past couple of years, that does not mean these constraint problems have gone away.

19. With the possibility of LNG supplies flowing into southern California, and other changes in the gas market, receipt point constraints may occur again at other receipt points.

20. Under the current system, end-users face uncertainty over whether their gas will flow through a constrained receipt point.

26. The FAR proposal will continue to provide market participants with flexible options and result in the creation of a citygate market for southern California.

27. The adoption of the FAR proposal provides certainty to FAR holders that their gas can be delivered from the receipt point to the citygate, which in turn will encourage parties to enter into long-term gas supply contracts.

28. The concerns regarding the FAR proposal's complexity, increased costs, and affiliate preference are unwarranted.

Contrary to these findings of fact and the Commission's claim that there is currently no citygate market, the SoCalGas system has a deep, highly liquid market consisting of all the receipt points for which SoCalGas accepts nominations. Although it is typically referred to as the SoCalGas "border" or "Topock" market, this is a citygate market, and it is working well under the protocol entitled "Scheduling and Allocation of Capacity on the SoCalGas System" ("SoCalGas Scheduling Protocol") that is posted on Envoy, the SoCalGas electronic bulletin board ("EBB"). Exhibit ("Ex.") 92, Attachment ("Att.") A (SCGC/Yap). SoCalGas' current system of nominations creates "unlimited flexibility" enabling shippers to shift "rapidly to the cheapest receipt points. *See* Ex. 44 at 7 (IP-CMTA/Beach); Transcript ("Tr.") 10/1489 (IP-CMTA/Beach); SCGC Brief at 4-6.

Neither SoCalGas in its initial proposal nor the Commission cites to any record evidence that establishes that there is or will be uncertainty with regard to end-users receiving their gas. The findings of fact relied upon the Commission are merely conjecture and not based on any actual evidence. As in *CMTA*, the Commission has not shown that FAR as approved is more likely to resolve the problems perceived by the Commission and SoCalGas than less onerous proposals, such as the Joint Proposal which was presented by liquefied natural gas developers, core customer representatives (The Utility Reform Network), and noncore customer representatives (SCGC).

First, there are only two zones in which there is a mismatch between receipt point capacity and takeaway capacity, the North Desert Transmission Zone ("NDTZ") and

Wheeler Ridge. The SoCalGas Scheduling Protocol provides specific rules for allocating zonal takeaway in both zones. For NDTZ, under the allocation methodology established in D.04-09-022 (Sep. 4, 2004), there has been only one cut in deliveries since Spring 2005, which is well within SoCalGas' definition of firm service, 97 percent reliability. *See* Ex. 92, Att. D at 6 (SoCalGas/SDG&E Response 6 to SCGC Data Request 12); Tr. 4/489 (SoCalGas-SDG&E/Morrow); SCGC Brief at 6-8 (*citing to* SDG&E and SoCalGas Reply Comment on ALJ's Draft Decision at 4 (Aug. 16, 2004); Ex. 92 at 16 (SCGC/Yap), Ex. 93 at 10 (SCGC/Yap)). Similarly, deliveries at Wheeler Ridge have been 98-99 percent firm. *See* SCGC Brief at 8-10. During 2005, there were only six days when there was full utilization of actual available capacity in the Wheeler Ridge Zone. Ex. 98; Tr. 14/2203 (PG&E/Graham).

Second, the FAR proposal as adopted merely creates a new paper "citygate" market at precisely the same place physically as the current southern California "border" market, the SoCalGas receipt points. The new citygate market would be separated from the existing citygate market only by the five-cent charge to be paid by market participants for gas that would then be deemed to be at the new citygate. The FAR system would divide the existing citygate market into two or more submarkets, decreasing the liquidity of the existing markets, to no apparent benefit of SoCalGas' shippers. Such a scheme is certainly to the benefit of SoCalGas, however, which stands to recover up to $70.7 million from FAR holders. *See* Ex. 93 at 17 (SCGC/Yap); Ex. 80 at 10 (Coral/Travis).

Third, even proponents of FAR acknowledge that comparing how PG&E's system of firm access rights is working with how the proposed FAR would work for SoCalGas is "disingenuous." *See, e.g.*, Hearing Tr. at 2427:25-28 (Ms. Kahl stating that "it's a little disingenuous to suggest that we should look at PG&E to find out what we should fear when

PG&E apparently isn't a very good model for SoCalGas"). Moreover, parties that rely on the fact that firm access rights are features of the PG&E system and most interstate pipeline systems have only one piece of the puzzle. Firm delivery and receipt point rights are generally not divorced from firm transportation rights. They are tied together in one system of operations. Both PG&E and interstate pipelines provide firm point-to-point transportation with firm receipt point rights and firm delivery point rights being associated with an allocation of firm transportation capacity rights on the pipeline. That is not what SoCalGas proposed nor what the Commission approved in D.06-12-031. The Commission approved a scheme of access rights without any transportation rights being linked to the access rights. Adopting access rights that are divorced from any physical transportation rights serves only to fragment the existing citygate market, increase costs to end-use customers for which the system was built, and benefit SoCalGas.

Finally, although the Commission is correct that one sort of FAR scheme or another has been considered over the last nine years, all have been rejected or delayed indefinitely while customers of SoCalGas continue to receive 98 to 99.9 percent firm service. There is simply no need for the FAR program to ensure that Californians receive the gas and the gas-fired electricity that they demand. The Commission should reject FAR and allow the market to continue functioning successfully without burdening end-users and other market participants with complex and onerous procedures in order to receive their gas.

### B. The Commission's Adoption of the FAR Program Is Contrary to California State Policy Regarding GHG Emissions.

Further evidence of the lack of a rational basis for approving the FAR program is provided by the conflict between approving FAR and California's policy of reducing GHG emissions. The Commission's adoption of the FAR program will make the operations of gas-fired EGs more complex, costly, and difficult precisely when gas-fired generation will be increasingly needed to back out coal and to firm the delivery of intermittent renewable resources. As the Commission recently observed, "policies that increase natural gas supply and lower natural gas costs help to address many of California's most critical environmental challenges." D.06-09-039, Rulemaking ("R.") 04-01-025 (Phase II) at 156 (Sep. 21, 2006). The Commission explained further:

> [T]he CPUC is aggressively pursuing policies to address the threat of climate change. The Commission is investigating adopting a greenhouse gas emissions performance standard for new electricity procurement contracts entered into by the investor-owned utilities that would limit greenhouse gas emissions to the level emitted by modern natural gas-fire generation. If the Commission determines that promoting gas-fired generation over other types of generation is necessary to achieve our climate change goals, then the Commission should clearly adopt policies that increase the supplies of natural gas needed to fuel these plants.

*Id.* . California's commitment to addressing the threat of climate change and to meeting the challenge of GHG emissions has been confirmed by the agreement of Governor Schwarzenegger and the California Legislature in Assembly Bill 32, the Global Warming Solutions Act of 2006 (Sep. 27, 2006), to cap the State's GHG emissions at 1990 levels by 2020.

Gas-fired generation contributes to GHG reduction by backing out coal-fired generation. Gas-fired generation also contributes by providing dispatchable capacity that can be used to firm deliveries of energy from intermittent renewable energy resources such as wind. Imposing access charges and the FAR market structure would conflict directly with California's GHG reduction policy. Although the Commission's focus should be on making it easier and less costly to burn gas, the Commission's approval of the FAR scheme would increase the roadblocks to gas-fired generation. The Commission's adoption of the FAR structure should be reversed, and the current market structure should be retained.

## IV. D.06-12-031 FAILS TO PROVIDE ANY JUSTIFICATION FOR SET-ASIDES GENERALLY, THEN FAILS TO PROVIDE A COHERENT BASIS FOR GRANTING SET-ASIDES THAT ARE CLEARLY DISCRIMINATORY.

In addition to the fact that the FAR program is unnecessary and that the access charge is illegal, the FAR program adopted by the Commission is fraught with serious problems. In accepting SoCalGas' proposed list of set-asides as well as most of the other parties' requests for set-asides, the Commission provides no systematic rationale for establishing set-asides. Instead, the Commission grants individual set-asides on an *ad hoc* basis. The bases for determining which customers should receive set-asides and the amount of the set-asides differ depending on the type of customer without explanation.

Without providing any reason for granting set-asides generally, the Commission approves set-asides for California producers and for core suppliers that have long-term upstream contracts, including the SoCalGas and SDG&E Gas Acquisition Departments. However, in a change from Administrative Law Judge ("ALJ") Wong's Proposed Decision ("PD"), the Commission rejects set-asides for noncore customers that hold long-term upstream transportation contracts. Similarly, without explanation in another change from the PD, the Commission approves producer set-asides that would be based on the peak month over the past three years rather than the monthly average over the past three years. Likewise, although there is a limit based on a rolling five-year average on the amount of capacity available for Steps 1 and 2 at each receipt point, the Commission approves set-asides in the SoCalGas Southern Zone that exceed that limit. These examples illustrate that the FAR set-asides have no clear underlying rationale to support them and conflict with other aspects of the FAR program.

### A. Denying Set-Asides to Noncore Customers that Have Long-Term Commitments to Upstream Capacity Is Discriminatory and Unsupported by the Record.

It is patently discriminatory for the Commission to deny set-asides to noncore customers that have commitments to upstream capacity while granting set asides to others that have such commitments. SoCalGas' core customers are granted a set-aside in Step 1 to match their qualifying upstream pipeline contracts. D.06-12-031 at 14. Likewise, Core Transportation Aggregators and wholesale customers serving core load are granted set-asides based on their qualifying upstream interstate pipeline commitments. *Id*. at 14-15. Holders of Commission-approved long-term firm contracts for upstream capacity on the Pacific Gas and Electric Company system are granted a set-aside. *Id*. at 94. California producers also receive a set-aside. *Id.* at 15. Other parties, including Exxon Mobil, Occidental of Elk Hills, Inc. ("OEHI"), and SCGC, requested set-asides either for their production or to match long-term contractual commitments to upstream capacity. The Commission granted all of the requests except one: SCGC's request for a set-aside for noncore customers with upstream interstate pipeline contracts was denied. *Id*. at 93-97.

In granting OEHI's request for a set-aside, the Commission noted SoCalGas' position that granting a set-aside to OEHI would disadvantage other pipeline deliveries in the heavily used Wheeler Ridge transmission zone as well as potential customers who want to obtain FAR in that zoned. D.06-12-031 at 93. However, the Commission determined that SoCalGas, PG&E, and OEHI contemplated that the Gosford interconnect would be used for OEHI's production, and that OEHI paid for the facilities. *Id*. The Commission concluded that OEHI should receive the benefit of its bargain. *Id*. at 94.

Likewise, Exxon Mobil received a set-aside for its offshore production. The Commission noted that SoCalGas had treated Exxon Mobil similar to the California producers, notwithstanding that it had a different type of contract. *Id*. at 94.

The Commission also granted set-asides for customers that hold Commission-approved transportation contracts for pipeline capacity on PG&E, despite SoCalGas' arguments that these customers did not sign those contracts with the expectation of receiving firm access to SoCalGas' system. D.06-12-031 at 94.

Furthermore, the Commission granted set-asides to LNG developers, including developers who would deliver gas through the Otay Mesa delivery point into the Southern Zone:

> If a funding party builds new capacity or expands existing capacity on a displacement basis at Otay Mesa, up to 700 MMcfd, and the funding party pays for it on an incremental basis, the funding party shall be eligible to receive a step 1 set-aside for firm rights in the Southern Zone at Otay Mesa in the open season for the amount of capacity that the funding party paid for.

D.04-12-031 at 74. The result is that the core set-aside for the Southern Zone plus the LNG developers' set-aside (480 MMcf/d at Ehrenberg and 400-700 MMcf/d at Otay Mesa) exceed the total amount of capacity available in Steps 1 and 2 for the Southern Zone, assuming that the Commission consistently applies the adopted five-year average limit on capacity to be made available in Steps 1 and 2 of the FAR bidding process. Nevertheless, the set-asides were granted.

It seems that the unstated purpose of the approved set-asides for shippers is to match as closely as possible each customer's commitment to upstream capacity, including production capacity, interstate pipeline capacity, and intrastate pipeline capacity. However, the Commission fails to create a comprehensive and cohesive scheme for set-asides, resulting in a discriminatory decision to single out and deny a set-aside for noncore customers that hold commitments to capacity on interstate pipelines.

In denying a set-aside for noncore customers that hold commitments to capacity on interstate pipelines, the Commission relies solely on a statement that granting set-asides for those noncore customers would be "likely to reduce the amount of capacity available to end-users at the most popular receipt points, and little, if any, capacity would be available to end-users and other market participants in Steps 2 and 3." D.06-12-031 at 95.[1] This is the basis for the Commission's apparent contention that the discrimination against noncore customers that hold commitments to upstream capacity is not undue discrimination.

There is no record support for the proposition that a set-aside for noncore customers that hold long-term commitments to upstream capacity would reduce the capacity at the "most popular receipt points" to "little, if any," capacity in Step 3 of the FAR open season. The California Manufacturers and Technology Association ("CMTA") presented a table in its comments on ALJ Wong's PD that purported to show the impact of the "EG set-aside." CMTA assumed that 75 percent of the capacity at each receipt point would be made available in Steps 1 and 2 of the FAR open season, as originally proposed by SoCalGas, and CMTA assumed that the capacity that SoCalGas proposed to be set aside in Step 1 would be taken by the set-aside beneficiaries. CMTA compared the amount that it claimed would be set aside for EGs to the amount of capacity at each receipt point that would then be available in Step 2 of the open season. CMTA's result was as follows:

[1] The Commission also mentions Watson/IP/CCC/CMTA's argument that noncore upstream contracts never contemplated firm service on SoCalGas. The Commission should not rely on this argument given that the G-FX customers also did not contemplate firm service on SoCalGas.

| IMPACT OF EG SET-ASIDE ON AVAILABLE STEP 2 CAPACITY | | | |
|---|---|---|---|
| Receipt Point | Step 2 Capacity Before EG Set-Aside | Potential EG Set-Aside | % Share |
| EPN Ehrenberg | 428 | 94 | 22% |
| EPN Topock | 125 | 51 | 40% |
| TW North Needles | 400 | 0 | 0% |
| TW Topock | 143 | 0 | 0% |
| QST at North Needles | 90 | 0 | 0% |
| KR Kramer Junction | 375 | 386 | 103% |
| KR/MP Wheeler Ridge | 494 | 393 | 80% |
| Oxy Gosford | 113 | 0 | 0% |
| PG&E Kern River Station | 340 | 13 | 4% |
| Line 85 | 20 | 0 | 0% |
| Coastal | 50 | 0 | 0% |
| **Total** | **2,576** | **937** | **36%** |

CMTA Comment, Table 1 (Nov. 20, 2006). As SCGC explained in it Reply Comment on ALJ Wong's PD, SCGC was unable to verify the numbers in CMTA's Table 1.

SCGC Reply Comment at 4. However, CMTA's own figures show that, on the basis of CMTA's own assumptions, there would be substantial capacity left in Step 2 for other customers at all receipt points except at Wheeler Ridge and Kramer Junction. At Wheeler Ridge, arguably the most popular point, 20 percent of the Step 2 capacity would still be available for others in Step 2, and all of the Step 3 capacity would remain available.

Kramer Junction would be the most constrained as a result of what CMTA claims would be the "EG set-aside." Kramer Junction is unique insofar as it is the receipt point of choice for EGs. Even there, using CMTA's numbers, while the EGs would take all of the Step 2 capacity, nearly all of the capacity that SoCalGas proposed to reserve for Step 3 bidding would remain available. Thus, no party, including CMTA, claimed that an "EG set-aside" would consume all of the Step 2 and Step 3 capacity at "the most popular receipt points," as erroneously claimed in D.06-12-031. There is absolutely no record support or even extra-record support for the proposition that a "set-aside for noncore customers who have long-term contract commitments on the upstream pipelines … [would be] likely to reduce the amount of capacity available to end-users at the most popular receipt points, and little, if any, capacity would be available to end-users and other market participants in Steps 2 and 3." D.06-12-031 at 95. That proposition is the sole basis for the Commission's discriminatory denial of a set-aside for noncore customers that hold commitments to upstream capacity, and the proposition is unfounded.

Even if the proposition were true, it would not provide an adequate basis for discriminating against noncore customers that hold commitments to upstream capacity.

If granting the requested set-aside would intrude on the last 25 percent of capacity at one or more receipt points and the Commission were to determine, on that basis, that the set-aside should be denied, the implication would be that non-end-user market participants have some right to use SoCalGas' system to the detriment of end-users that have paid for the system and for which the system was built. However, as discussed further below, the Commission fails to provided any explanation about why capacity should be reserved for bidding in Step 3 or why end-users should be forced into bidding against marketers for firm access rights. As a result of the failure to provide any rationale for reserving capacity for Step 3 bidding, the reservation of capacity for Step 3 is arbitrary and capricious and unsupported by reasoned decision-making.

Insofar as the denial of a set-aside to noncore customers that hold commitments to upstream capacity is unsupported by the record, the discrimination is undue and is arbitrary and capricious. On rehearing, the denial of the requested set aside should be recovered or the entire scheme of set-asides should be rejected.

### B. Basing Set-Asides for Producers on a More Generous Standard than Bidding Rights for Other Customers Is Arbitrary and Discriminatory.

In approving the set-asides for California gas producers in D.06-12-031, the Commission, without explanation, diverges from ALJ Wong's PD and bases the producer set-asides on the individual historical peak month over the most recent three-year period. D.06-12-031 at 100. The PD based the producer set-asides on an individual producer's average monthly production over the most recent three-year period. PD at 97. The PD also provided that noncore customer Step 2 bidding rights would be based on a customer's average monthly production over the most recent three-year period. PD at 101. Thus, the PD established parity between treatment of the producers and treatment of the noncore customers.

If the standard for establishing the producers set-asides is to be liberalized, the standard for setting the Step 2 bidding rights should be liberalized, as well. D.06-12-031 still requires that end-use customers' bids shall be limited to historical average usage over the past three years. D.06-12-031 at 104. To maintain parity with the producers, noncore customer Step 2 bidding rights should be based on customer's peak month volumes over the most recent three year period.

### C. Basing Set-Asides for Parties that Build on a Displacement Basis at Otay Mesa on a More Generous Standard than the Set-Asides for Other Displacement Customers Is Arbitrary and Discriminatory.

In granting set-asides for FAR holders that build displacement capacity, the Commission granted set-asides at Otay Mesa in the Southern Zone based on a more generous standard than the set-asides for building displacement capacity at other receipt points in other zones. With regard to Otay Mesa, the Commission provided:

> If a funding party builds new capacity or expands existing capacity on a displacement capacity basis at Otay Mesa, up to 700 MMcfd, and the funding party pays for it on an incremental cost basis, the funding party shall receive a Step 1 set aside at Otay Mesa in the open season for the capacity that the funding party paid for.

D.06-12-031 at 75. However, for other receipt points, the Commission limited the set-aside that would be provided to funding parties:

> If the funding party builds new capacity or expands existing capacity on a displacement capacity basis, and the funding party pays for it on an incremental cost basis, the funding party shall receive a Step 1 set-aside for the capacity that the funding party paid for, *but that set-aside shall be subject to nominations at other receipt points in the same transmission zone*.

*Id*. at 74 (emphasis added). Thus, under the FAR proposal as adopted in D.06-12-031, both holders of FAR in the Southern Zone and holders of FAR elsewhere that pay for capacity expansions on a "displacement" basis would be eligible for a Step 1 set-aside and would pay the same firm access charge, but the set-aside for funding parties that paid for expansion capacity on a "displacement" basis in zones other than the Southern Zone would be subject to prorationing. D.06-12-031 provides for this discriminatory treatment but fails to provide any explanation or rationale for the discrimination. As a result of that failure, the discrimination is undue as well as arbitrary and capricious. Either the discrimination should be explained, or it should be eliminated as undue.

## V. D.06-12-031 ERRS IN APPROVING THE PREFERENCE FOR ANNUAL BIDS OVER SEASONAL BIDS ON THE BASIS THAT ELECTRIC GENERATORS RECEIVE SET-ASIDES.

Having rejected set-asides for EGs that hold upstream commitments, purportedly to ensure that other market participants can access the most popular receipt points, the Commission bizarrely relies upon a presumption that it has *granted* a Step 1 set-aside to EGs that hold upstream capacity commitments as the basis for rejecting SCGC's request to eliminate the FAR proposal's preference for annual bids over seasonal bids.

SCGC had argued that SoCalGas' proposed preference for baseload or annual bids over monthly or seasonal bids for Step 2 capacity favors utility interests rather than customer interests and should be rejected. The likely consequence of a preference for baseload bids in Step 2 and a requirement of baseload bids in Step 3 would be that an EGs would be confronted with the

Hobson's choice of (1) taking FAR on an annual "baseload" basis, which would increase the unit cost of gas transmission capacity for low load factor EGs, or (2) relying on a mix of interruptible access rights and citygate purchases which could degrade reliability and raise the cost of natural gas service to EGs. Either way, the ultimate consequence of SoCalGas' proposed performance would be to increase the cost of electricity to electric ratepayers.

In rejecting SCGC's concerns, the Commission stated that "with the set-aside for the upstream contracts of EGs, they should be able to obtain most, if not all, of what they need." D.06-12-031 at 104. However, the Commission *rejected* set-asides for EGs, which will now be required to bid on capacity in Step 2 and, most likely, in Step 3. If the Commission fails on rehearing to grant a Step 1 set aside to noncore customers that hold commitments to upstream capacity, the Commission should eliminate the preference for annual or baseload bids in Steps 2 and 3.

## VI. D.06-12-031 ARBITRARILY LIMITS THE AMOUNT OF RECEIPT POINT CAPACITY TO BE MADE AVAILABLE IN STEPS 1 AND 2 IN ORDER TO RESERVE CAPACITY FOR STEP 3.

SoCalGas originally proposed limiting the capacity that would be made available in Steps 1 and 2 of the FAR bidding process to 75 percent of the capacity at each receipt point.. SoCalGas' rationale was that this percentage is approximately equal to the estimated 2004 consumption divided by 3,656 MMcf/d of non-California backbone takeaway capacity. Ex. 12 at 11, n. 10 (SoCalGas/Watson).

D.06-12-031 rejects the 75 percent limitation on capacity to be made available in Steps 1 and 2. Instead, the Commission limits Step 2 capacity to the historical utilization by month at each individual receipt point using a rolling five-year average, less any Step 1 set-asides. D.06-12-031 at 103. The Commission's rationale for limiting the amount of capacity that would be made available in Step 2 is "that end-use customers who pay for the transmission costs in their rates should get what they pay for." *Id.* However, the Commission also noted that "the FAR system should provide all market participants with the opportunity to obtain FAR." *Id*.

Imposing a limit on the capacity available in Steps 1 and 2 is inconsistent with limiting an individual customer's bidding rights in Step 2. The Commission attempts to rationalize the Steps 1 and 2 capacity limit by stating that marketers and other market participants should be allowed access to the Commission's newly created alternate citygate market. However, the Commission itself recognizes that: "The transmission system has been paid for in rates by the end-users of SDG&E and SoCalGas." Finding of Fact 30, D.06-12-031 at 121. If the customers have paid for the system, and customers' bidding rights are limited to their historical usage, there should not also be a limit on the amount of receipt point capacity that is made available in Steps 1 and 2.

The Commission should eliminate the overall limit on the capacity available in Steps 1 and 2. If the Commission limits bids in Step 2 to historical usage, that limitation should be sufficient to ensure that other market participants will have the opportunity to participate in the southern California market while simultaneously ensuring that existing customers access to capacity what they already have paid for.

## VII. D.06-12-031 FAILS TO LIMIT BIDS FOR EXISTING CAPACITY IN STEP 3 TO THREE-YEAR TERMS.

The Commission determined that "Step 3 should take place in two bidding stages, one for existing capacity remaining after Step 2, and one for expansion and new capacity." D.06-12-031 at 105. However, although the Commission noted that a minimum three-year contract term in Step 3 would be consistent with the contract terms in Steps 1 and 2, the Commission only stated that it would permit the contract term in Step 3 to "range from three years to 20 years" *Id.* The Commission should rehear this issue and clarify that the contract term for *existing capacity* awarded in Step 3 is three years, consistent with the contract terms in Steps 1 and 2.

## VIII. THE FIVE-CENT "UNBUNDLED" RESERVATION CHARGE IS NOT BASED ON ANY COST EVIDENCE AND IS ARBITRARY AND CAPRICIOUS.

SoCalGas originally proposed to charge a five-cent access charge in order to prevent hoarding of FAR. This charge was not based on unbundling backbone transmission costs from transportation rates. The Commission acknowledged that 15.75 cents/dth is the estimate of the backbone transmission costs. However, the Commission found that "[a] reservation charge lower than the unbundled FAR proposal rate of 15.75 cents per Dth is needed to stimulate participation for holding a FAR." Finding of Fact 34, D.06-12-031 at 136.

If the FAR program were truly necessary and deemed valuable, the Commission would not have to stimulate participation in the new FAR market by adopting an arbitrary five-cent charge. Commissioner Chong recognized the problems with the five-cent charge in her statement at the Commission meeting approving D.06-12-031:

> The five-cent FAR charge that we put in place today could be subject to criticisms that it's non-cost-based and arbitrary and capricious. Thus, SoCalGas and SDG&E are directed to perform the studies necessary to establish a cost-based charge in their upcoming BCAP. We do want this cost-based rate in place *prior* to the second three-year open season.

Statement of Commissioner Chong, December 14, 2006 Commission Meeting. Insofar as the five-cent FAR charge is not cost-based and is unsupported by evidence, it is arbitrary and capricious. The five-cent access charge should be rejected and set to zero, or FAR implementation should be delayed until after the next BCAP, when the Commission can review SoCalGas' and SDG&E's cost data to establish a cost-based FAR charge.

## IX. D.06-12-031 APPEARS TO PREJUDGE THE BCAP WHICH IS TO COMMENCE IN 2007.

The Commission, recognizing that D.06-12-031 "marks a significant change to the basic structure of the natural gas market … and will result in an unbundled element in SoCalGas' rates" D.06-12-031 (at 132) requires SoCalGas to file its BCAP application no earlier than October 1, 2007, and no later than December 15, 2007. However, the Commission appears to have determined the outcome of the BCAP before it has begun.

Before the Commission has had a chance to review the extent of the cost shifting among customers that D.06-12-031 will require, the Commission orders that in its next BCAP application, SoCalGas shall "include a proposal for a total redesign of its rate consistent with the discussion regarding closing or minimizing the regulatory gap." *Id.* at 143. The Commission further orders that "[u]pon closing of the regulatory gap, the existing peaking service tariff shall sunset at the conclusion of the next BCAP." *Id*.

The Commission has already acknowledged that shifting the full unbundled cost of the backbone transportation to a large demand charge will act as a deterrent to obtaining FAR. *Id*. at 85 ("the 15.75 cents reservation charge, which approximates the noncore's backbone transmission costs, is likely to act as a deterrent to those market participants who want FAR"). The Commission has not fully addressed cost-shifting issues in this proceeding. Nor does the Commission have facts to make a determination that the supposed "regulatory gap" should be closed in the next BCAP by adopting substantial demand charges for gas transmission service. The Commission should make it clear that it is not prejudging the outcome of SoCalGas' and SDG&E's next BCAP proceedings and that all cost-shifting and rate design issues will be impartially examined in that proceeding.

## X. CONCLUSION.

For the reasons set forth above, SCGC requests that the Commission grant rehearing and, upon rehearing, take the following actions:

- Reject SoCalGas' FAR proposal in its entirety.
- If FAR is not rejected, design a system of firm transportation rights that are consistent with federal law.
- If FAR is not rejected, revise D.06-12-031 to set forth findings of fact and conclusions of law that provide a rational basis for approving a system of firm rights.
- If the Commission, upon rehearing, revises D.06-12-031 to set forth findings of fact and conclusions of law that provide a rational basis for approving a system of firm transportation rights:

  (1) define the purpose for which set-asides should be established and establish a non-discriminatory method for determining set-asides, or eliminate set-asides altogether;

  (2) reject the preference for annual bids over monthly bids in Step 2;

  (3) eliminate the arbitrary five-year average limitation on the amount of capacity that may be set aside in Step 1 and bid upon in Step 2 of the FAR bidding process;

  (4) limit bids for existing capacity in Step 3 to three-year terms;

  (5) eliminate the five-cent "unbundled" access charge or defer implementation of the FAR program until after the next SoCalGas BCAP; and

(6) make it clear that D.06-12-031 is not predetermining the outcome of SoCalGas' and SDG&E's next BCAP proceedings.

Respectfully submitted,

*/s/ T. Alana Steele*

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Dated: January 16, 2007

# CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the **SOUTHERN CALIFORNIA GENERATION COALITION APPLICATION FOR REHEARING** on the service list for A.04-12-004, by serving a copy to each party by electronic mail, or by mailing a properly addressed copy by first-class mail with postage prepaid to each party unable to accept service by electronic mail.

Executed on January 16, 2007, at Los Angeles, California.

*/s/ Rosemarie F. McBride*

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